FILE COPY

FILED
SEP 24 193
CHARLES ELMORE CROPLEY
CLERK

In the Supreme Court of the United States

OCTOBER TERM, 1934

No. 6

GUY T. HELVERING, COMMISSIONER OF INTERNAL REVENUE,
Petitioner,

v.

SUSAN DWIGHT BLISS

BRIEF AS AMICUS CURIAE ON BEHALF OF ROBERT TREAT PAINE, 2ND

PHILLIPS KETCHUM,
Counsel for Robert Treat Paine, 2nd.
1 Federal Street,
Boston, Massachusetts.

BOSTON
PRESS OF GEO. H. ELLIS CO.
INCORPORATED
1934

INDEX

PAGE

I. PRELIMINARY STATEMENT AS TO INTEREST OF ROBERT TREAT PAINE, 2ND 1

II. QUESTION INVOLVED 2

III. THE FACTS 2

IV. THE STATUTE 4

V. THE ARGUMENT 8

A. The term "net income" as used in Section 23(*n*) of the Revenue Act of 1928 (the Section limiting to 15 per centum of the taxpayer's "net income" the deduction for charitable gifts) means the net income as defined by Sections 21, 22, and 23, and includes capital net gain

B. Even if it might be thought good public policy to exclude *capital net loss* in computing the amount of the charitable deduction, nevertheless it would be most poor public policy and inconsistent with the purpose of the Revenue Act to exclude *capital net gain* in computing the amount of the charitable deduction 9

VI. CONCLUSION 15

CITATIONS

CASES

	PAGE
Bliss, Susan Dwight v. *Commissioner*, 27 B. T. A. 205	3
Bliss v. *Commissioner of Internal Revenue*, 68 Fed. 2nd 890	3
Elkins, Hallie D. v. *Commissioner*, 24 B. T. A. 572	9
Livingood, Charles J., Executor v. *Commissioner*, 25 B. T. A. 585	9
Straus, Aaron v. *Commissioner*, 27 B. T. A. 1116	10

STATUTES

Act of Congress, October 3, 1917 (Revenue Act of 1917)	10
Act of Congress, February 24, 1919 (Revenue Act of 1918)	11
Act of Congress, November 23, 1921 (Revenue Act of 1921)	11, 12
Act of Congress, May 29, 1928 (Revenue Act of 1928)	4–8

In the Supreme Court of the United States

OCTOBER TERM, 1934

No. 6

GUY T. HELVERING, COMMISSIONER OF INTERNAL REVENUE, *Petitioner*,

v.

SUSAN DWIGHT BLISS

BRIEF AS AMICUS CURIAE ON BEHALF OF ROBERT TREAT PAINE, 2ND

I

PRELIMINARY STATEMENT AS TO INTEREST OF ROBERT TREAT PAINE, 2ND

Robert Treat Paine, 2nd, is the claimant in a claim for refund of excessive federal income tax paid by him in the year 1930. This claim for refund was filed by Paine with the Collector of Internal Revenue at Boston on June 14, 1933, and is now pending.

The principal issue in this claim for refund is similar to that in the *Bliss* case and involves a construction of Section 23(*n*) of the Revenue Act of 1928, which provides that, in computing taxable net income, charitable gifts shall be allowed as deductions from gross income to an amount not

in excess of 15 per centum of the taxpayer's "net income," as computed before any allowance for charitable gifts.

In the year 1930 the net income of Robert Treat Paine, 2nd, was made up entirely of capital net gain; the "ordinary deductions" (not including any allowance for charitable gifts) having been in excess of the "ordinary income." In that year Paine made charitable gifts (of a kind deductible under Section 23(*n*) of the Statute) amounting to $8,707.00, which amount was less than 15 per centum of his taxable net income including capital net gain. The Commissioner, in adjustment of Paine's 1930 income tax, disallowed all of said gifts as a deduction, as a result of which disallowance Paine filed claim for refund as aforesaid.

The issue here raised also affects Paine's income tax liability for other years.

II

QUESTION INVOLVED

The question involved is: does the term "net income," as used in said Section 23(*n*) of the Revenue Act of 1928, include net gains from the sale of investment property held for more than two years (*i.e.*, denominated "capital net gains" in Section 101(*c*)(5) of the 1928 Act), or should such capital net gains be excluded in computing said "net income"?

III

THE FACTS

The *Blair* case involves the years 1928 and 1930. The issue as to the amount allowable as a deduction for charitable gifts is common to both taxable years. It will suffice, therefore, to state the facts with reference to the year 1928 only.

During the year 1928 Susan D. Bliss made charitable gifts of $43,995.92. Her total net income in that year (before any allowance for charitable gifts) was $482,035.59, comprised of $270,490.77 "ordinary net income" (before any allowance for charitable gifts) and $211,544.82 "capital net gain" (before any allowance for charitable gifts). The Commissioner of Internal Revenue allowed as a deduction for charitable gifts the sum of $40,573.62, being 15 per centum of her "ordinary net income" (before any allowance for charitable gifts) and disallowed as a deduction the balance of her charitable gifts ($3,422.30). As a result the Commissioner determined a tax deficiency in the year 1928 in the amount of $1,909.31.

On an appeal, the Board of Tax Appeals sustained the Commissioner in refusing to allow as a deduction for charitable gifts an amount in excess of 15 per centum of the taxpayer's "ordinary net income."

> *Susan Dwight Bliss* v. *Commissioner*, 27 B. T. A. 205 (Dec. 2/32. Overruled by Board of Tax Appeals in *Aaron Straus* v. *Commissioner*, 27 B. T. A. 1116, April 6/33).

On an appeal, the Circuit Court of Appeals for the Second Circuit reversed the decision of the Board of Tax Appeals, holding that the taxpayer was entitled to compute the charitable deduction on the basis of her net income, *including* therein capital net gain.

> *Bliss* v. *Commissioner of Internal Revenue*, 68 Fed. 2nd 890 (C. C. A. 2nd, Jan. 8, 1934).

From the foregoing decision of the Circuit Court of Appeals, the Commissioner has brought the petition with respect to which this brief is filed.

IV

THE STATUTE

The pertinent portions of the Revenue Act of 1928 are as follows:

* * * * * * *

"TITLE I—INCOME TAX

SUBTITLE B—GENERAL PROVISIONS

PART II—COMPUTATION OF NET INCOME

SEC. 23. DEDUCTIONS FROM GROSS INCOME. In computing net income there shall be allowed as deductions . . .

(*n*) Charitable and Other Contributions. In the case of an individual, contributions or gifts made within the taxable year to or for the use of:

(1) the United States, any State, Territory, or any political subdivision thereof, or the District of Columbia, for exclusively public purposes;

(2) any corporation, or trust, or community chest, fund, or foundation, organized and operated exclusively for religious, charitable, scientific, literary, or educational purposes, or for the prevention of cruelty to children or animals, no part of the net earnings of which inures to the benefit of any private shareholder or individual;

(3) the special fund for vocational rehabilitation authorized by Section 7 of the Vocational Rehabilitation Act;

(4) posts or organizations of war veterans, or auxiliary units or societies of any such posts or organizations, if such posts, organizations, units, or societies are organized in the United States or any of its possessions, and if no part of their net earnings inures to the benefit of any private shareholder or individual; or

(5) a fraternal society, order, or association, operating under the lodge system, but only if such contributions or gifts are to be used exclusively for religious, charitable, scientific, literary, or educational purposes, or for the prevention of cruelty to children or animals;

to an amount which in all the above cases combined does not exceed 15 per centum of the taxpayer's net income as computed without the benefit of this subsection. Such contributions or gifts shall be allowable as deductions only if verified under rules and regulations prescribed by the Commissioner, with the approval of the Secretary. (For unlimited deduction if contributions and gifts exceed 90 per centum of the net income, see Section 120.)" (Italics supplied.)

* * * * * * *

"TITLE I—INCOME TAX
SUBTITLE B—GENERAL PROVISIONS
PART II—COMPUTATION OF NET INCOME

*SEC. 21. NET INCOME. 'Net income' means the gross income computed under Section 22, less the deductions allowed by Section 23.

**SEC. 22. GROSS INCOME. (*a*) General definition. 'Gross income' includes gains, profits, and income derived from salaries, wages, or compensation for personal service, of whatever kind and in whatever form paid, or from professions, vocations, trades, businesses, commerce, *or sales, or dealings in property,* whether real or personal, growing out of the ownership or use of or interest in such property; also from interest, rent, dividends, securities, or the transaction of any business carried on for gain or profit, or gains or profits and income derived from any source whatever. . . . . .

(*c*) Determination of Gain or Loss. In the case of a sale or other disposition of property, the gain or loss shall be computed as provided in Sections 111, 112, and 113. . . .

***SEC. 23. DEDUCTIONS FROM GROSS INCOME. In computing net income there shall be allowed as deductions:

(*a*) Expenses .....;
(*b*) Interest .....;
(*c*) Taxes Generally .....;
(*d*) Taxes of Shareholder Paid by Corporation;

* Sec. 21, Act of Cong., May 29, 1928, c. 852; 45 Stat. 797.
** Sec. 22, Act of Cong., May 29, 1928, c. 852; 45 Stat. 797.
*** Sec. 23, Act of Cong., May 29, 1928, c. 852; 45 Stat. 797, 799.

(*c*) Losses by Individuals. In the case of an individual, losses sustained during the taxable year and not compensated for by insurance or otherwise—

(1) if incurred in trade or business; or

(2) if incurred in any transaction entered into for profit, though not connected with the trade or business; or

(3) of property not connected with the trade or business, if the loss arises from fires, storms, shipwreck, or other casualty, or from theft.

(*f*) Losses by corporations.....;
(*g*) Basis for determining loss.....;
(*h*) Loss on sale of stock or securities.....;
(*i*) Net Losses .....;
(*j*) Bad debts .....;
(*k*) Depreciation .....;
(*l*) Depletion .....;
(*m*) Basis for depreciation and depletion....;
**(*n*) Charitable and other contributions.....;
(*o*) Future expenses in case of casual sales of real property .....;
(*p*) Dividends received by corporations.....;
(*q*) Pension trusts . . ." (Italics supplied).

* * * * * * *

"TITLE I—INCOME TAX

SUBTITLE C—SUPPLEMENTAL PROVISIONS

(supplementary to Subtitle B, Part I*)

*** SEC. 101. CAPITAL NET GAINS AND LOSSES.

(*a*) Tax in Case of Capital Net Gain. In the case of any taxpayer, other than a corporation, who for any taxable year derives a capital net gain (as hereinafter defined in this section), there shall, at the election of the taxpayer, be levied, collected, and paid, in lieu of all other taxes imposed by this title, a tax determined as follows: a partial tax shall first be computed upon the basis of the ordinary net income at the rates and in the manner as if this section had not been enacted and the total tax shall be this amount plus 12½ per centum of the capital net gain.

---

* "Rates of Tax." ** Quoted above, pp. 4–5.

*** Sec. 101, Act of Cong., May 29, 1928, c. 852; 45 Stat. 797, 811.

(*b*) Tax in Case of Capital Net Loss. In the case of any taxpayer, other than a corporation, who for any taxable year sustains a capital net loss (as hereinafter defined in this section), there shall be levied, collected, and paid, in lieu of all other taxes imposed by this title, a tax determined as follows: a partial tax shall first be computed upon the basis of the ordinary net income at the rates and in the manner as if this section had not been enacted, and the total tax shall be this amount minus 12½ per centum of the capital net loss; but in no case shall the tax of a taxpayer who has sustained a capital net loss be less than the tax computed without regard to the provisions of this section.

(*c*) Definitions. For the purposes of this title—

(1) 'Capital gain' means taxable gain from the sale or exchange of capital assets consummated after December 31, 1921.

(2) 'Capital loss' means deductible loss resulting from the sale or exchange of capital assets.

(3) 'Capital deductions' means such deductions as are allowed by section 23 for the purpose of computing net income, and are properly allocable to or chargeable against capital assets sold or exchanged during the taxable year.

(4) 'Ordinary deductions' means the deductions allowed by Section 23 other than capital losses and capital deductions.

(5) 'Capital net gain' means the excess of the total amount of capital gain over the sum of (A) the capital deductions and capital losses, plus (B) the amount, if any, by which the ordinary deductions exceed the gross income computed without including capital gains.

(6) 'Capital net loss' means the excess of the sum of the capital losses plus the capital deductions over the total amount of capital gain.

(7) 'Ordinary net income' means the net income, computed in accordance with the provisions of this title, after excluding all items of capital gain, capital loss, and capital deductions.

(8) 'Capital assets' means property held by the taxpayer for more than two years (whether or not

connected with his trade or business), but does not include stock in trade of the taxpayer or other property of a kind which would properly be included in the inventory of the taxpayer if on hand at the close of the taxable year, or property held by the taxpayer primarily for sale in the course of his trade or business. For the purposes of this definition—. . . . . .

(*d*) Collection and Payment of Tax. The total tax determined under subsection (*a*) or (*b*) shall be collected and paid in the same manner, at the same time, and subject to the same provisions of law, including penalties, as other taxes under this title."

V

THE ARGUMENT

A.

THE TERM "NET INCOME" AS USED IN SECTION 23(*n*) OF THE REVENUE ACT OF 1928 (THE SECTION LIMITING TO 15 PER CENTUM OF THE TAXPAYER'S "NET INCOME" THE DEDUCTION FOR CHARITABLE GIFTS) MEANS THE NET INCOME AS DEFINED BY SECTIONS 21, 22, AND 23 AND INCLUDES CAPITAL NET GAIN.

It was the uniform administrative practice of the Commissioner of Internal Revenue to allow charitable gifts as deductions to the limit of 15 per centum of the taxpayer's total net income, including capital net gain, from 1921, when the capital net gain provisions were originally adopted, until 1932, when the Commissioner reversed his position.

The argument as to the clear meaning of the term "net income," as used in Section 23(*n*) of the Revenue Act of 1928 (the Section limiting the deduction for charitable gifts to 15 per centum of the taxpayer's "net income"), has been fully and convincingly made in the briefs filed by counsel

for the respondent and by counsel for Aaron Straus, as *amicus curiae*. It would be surplusage to repeat that argument here.

The purpose of this brief is to draw the attention of the Court to an additional consideration, set forth in subsection B below.

B.

EVEN IF IT MIGHT BE THOUGHT GOOD PUBLIC POLICY TO EXCUDE *CAPITAL NET LOSS* IN COMPUTING THE AMOUNT OF THE CHARITABLE DEDUCTION, NEVERTHELESS IT WOULD BE MOST POOR PUBLIC POLICY AND INCONSISTENT WITH THE PURPOSE OF THE REVENUE ACT TO EXCLUDE *CAPITAL NET GAIN* IN COMPUTING THE AMOUNT OF THE CHARITABLE DEDUCTION.

In 1931 the Board of Tax Appeals was called upon to decide whether, in computing the charitable gift deduction under Section 23(*n*) of the 1928 Act, capital net loss should be included in or excluded from "net income."

> *Hallie D. Elkins* v. *Commissioner*, 24 B. T. A. 572 (Nov. 3/31).

This was the first time that the question of the exclusion from "net income" of either capital net loss or capital net gain had been presented to the Board. The Board decided that *capital net loss should be excluded from "net income"* in computing the charitable gift deduction.

This decision was followed by the Board, without substantial comment, in *Charles J. Livingood, Executor* v. *Commissioner*, 25 B. T. A. 585 (Feb. 23/32). These two Board decisions, which never have been followed in any decision of a higher court, were rendered long before the full Board (reversing the prior decisions of single members) held that *capital net gain should be included in "net income"* in computing the charitable gift deduction.

Aaron Straus, Petitioner v. *Commissioner*, 27 B. T. A. 1116 (April 6/33).

In deciding the *Straus* case, the Board stated that "the cases involving capital net losses may or may not be distinguishable from those involving capital net gains. We express no opinion on that subject . . ." (p. 1119).

The Board's decisions in the *Elkins* and *Livingood* cases have focussed attention on the handling of capital net loss in connection with the charitable gifts deduction. From these decisions the thought has arisen that it might be good public policy to allow a taxpayer, in years when he suffers large capital net losses, to retain his charitable gifts deduction unimpaired (*i.e.*, to exclude capital net loss in computing the net income on which said deduction is based). As perhaps a natural consequence of this consideration, some persons may assume that it would not be unreasonable or against public policy to exclude capital net gain in computing such net income. The purpose of this brief is to demonstrate that not to include capital net gain in computing such net income would be, in fact, opposed to public policy and inconsistent with the general theory of the Statute.

In presenting that argument, it is proper to review the sequence of, and the essential reasons for, the statutory provisions relating to the charitable gifts deduction and to capital net gain.

The provision relating to the charitable gifts deduction first appeared in federal revenue legislation in the Revenue Act of 1917.* The reason for the provision may be stated as follows. Congress realized that the higher income tax rates imposed by the new Act upon net income would obviously leave taxpayers with so much less income than in prior years that, unless some deduction was allowed for charitable gifts, taxpayers might curtail or omit their gifts to

---

* Revenue Act of 1917, Title XII, sec. 1201 (2); sec. 1201 (2), Act of Cong., October 3, 1917, c. 63; 40 Stat. 300, 330.

charity, thereby threatening the existence of charities and possibly throwing the burden of supporting charities upon the state. To relieve such a situation, the deduction for charitable gifts was permitted. The broad effect of the provision, therefore, was to exempt from income tax income given to charity and allowed to be deducted.

The limitation of the deduction to 15 per centum of the net taxable income, without the deduction, was obviously intended to prevent taxpayers from reducing their taxes by greatly increasing their charitable gifts. It was reasonable to suppose that the average person would not normally give to charity more than 15 per centum of his net taxable income.

Under the Revenue Act* in effect before the introduction in 1921 into federal revenue legislation of capital net gain provisions, there were two classes of net taxable income each subject to different rate of tax, namely, net income subject to both normal and surtax and net income subject to surtax only. Also, of course, different portions of the net income subject to surtax were taxable at differing rates of tax. The charitable gift deduction, however, was allowed to the extent of 15 per centum of all net taxable income of both classes, even though, as a result, such deduction might reduce, by much more than 15 per centum, the net income subject to both the normal and surtax and might offset entirely that portion of the net income subject to the highest rate of surtax. In other words, the taxpayer was allowed to take his deductible charitable gifts out of that part of his taxable income which was subject to the heaviest tax.

The Revenue Act of 1921 first introduced the capital net gain provision.** This provision in effect created, for the purpose of determining the rate of tax, a third class of net taxable income.

---

* Revenue Act of 1918; Act of Cong., February 24, 1919, c. 18; 40 Stat. 1057.

** Revenue Act of 1921, sec. 206; sec. 206, Act of Cong., November 23, 1921, c. 136; 42 Stat. 227, 232.

The Government's position is that this third class of net taxable income, which, in the case of persons with very large incomes, may be taxed at a much lower rate than prior to the Revenue Act of 1921, should not be included in figuring the percentage of net taxable income which may be devoted to deductible charitable gifts.

This contention is not reasonable. Prior to 1921 the tax law had allowed the charitable gifts deduction up to 15 per centum of all net taxable income (including profits on sales of securities), however taxed. There was nothing in the capital net gain provisions, as adopted in 1921,* to show that Congress intended to cut down the amount which taxpayers might give to charity free of tax.

Furthermore, it is more reasonable to assume that Congress intended that the charitable gifts deduction of up to 15 per centum of all classes of net taxable income (including capital net gain) should continue to be deductible, as previously, from net income taxable at the highest rate, rather than to assume that Congress intended suddenly (by discontinuing altogether the allowance of 15 per centum of capital net gain) to reduce the charitable deduction.

It may be surmised that the Government would never have suggested that all classes of net taxable income, at whatever rate taxed, should not be included in figuring the 15 per centum limitation for deductible charitable gifts, had it not been for the above-mentioned decision in the *Elkins* case (holding that capital net loss should not be deducted from net taxable income in figuring the allowable amount of deductible charitable gifts).

The *Elkins* decision was probably influenced by public policy. It is desirable that private charities be continuously supported by the gifts of private individuals. Many private individuals desire to continue their charitable gifts in spite of capital losses. They should be encouraged so to do. Accordingly, it would be a desirable thing that they be allowed

---

* Revenue Act of 1921, sec. 206; sec. 206, Act of Cong., November 23, 1921, c. 136; 42 Stat. 227, 232.

to deduct charitable gifts up to 15 per centum of their ordinary net income, regardless of their capital losses.

But to say that the result of the *Elkins* decision is in line with a wise public policy and is desirable is not the same thing as to say that the *Elkins* decision is legally correct under the Revenue Act of 1928. Nor is it to say that the rule of the *Elkins* case, which concerned capital net loss, would be, when applied to capital net gain, in line with wise public policy and desirable. In fact, the exact contrary is true.

The idea behind the *Elkins* decision is not reversible. Merely because a person should be encouraged to continue to give to charitable organizations 15 per centum of his ordinary net income in years when he has capital net losses, does not lead to the idea that he should be discouraged from giving to charitable organizations 15 per centum of his capital net gain in years when he has capital net gain. Before the Revenue Act of 1921, he was allowed by statute to deduct 15 per centum of his capital profits (unless diminished by other deductions) and give the same to charity tax-free. If the Government's present contention is sustained, the taxpayer will be deprived of that much of his charitable deduction.

The Government may say that the taxpayer should be deprived thereof, because, in the case of persons with very large incomes, the Revenue Act of 1921 (and subsequent Acts) greatly reduced the tax on capital net gains and so left taxpayers more able than before to make charitable gifts. This is not a valid argument for two reasons.

(1) The theory of the charitable gifts deduction is obviously to afford relief to generously-disposed taxpayers by allowing 15 per centum of their net taxable income to go tax-free to charity and by allowing the amount so given to charity to be deducted from the net income which would otherwise be taxed at the highest rate. Whereas a reduction in the rate of their taxes makes the need of this relief less urgent, it does not do away with the primary need of such relief.

(2) There are many persons of moderate incomes who under the capital net gain provision pay nearly as much tax on their capital net gains as under the other provisions of the law they pay on their ordinary incomes. For them the capital net gain provision is a minor, not a major, relief. Arbitrarily to attach to that relief a provision that they can no longer deduct 15 per centum of capital net gain for charitable gifts would be, through the financial burden on them, a direct interference with the public policy of promoting the continuance of their charitable gifts.

Congress might with some technical logic have adopted a plan of allowing charitable gifts (*a*) to be deducted from fully taxable net income up to 15 per centum of that income, (*b*) to be deducted from net income subject to surtax only up to 15 per centum of that income, and (*c*) to be deducted from capital net gain up to 15 per centum of such capital net gain. Congress might also have divided the deduction between the incomes subject to different rates of surtax. But Congress adopted no such plan. The plan's complication was a good reason weighing against its adoption.

Since such a plan was not adopted, it is much more reasonable to allow charitable gifts up to 15 per centum of net taxable income of all classes to be deducted from the income which would otherwise be taxed at the highest rate (by denying the appeal in this case) than to reduce the amount of the deduction by excluding capital net gain from the net income on which the 15 per centum limitation is figured (by applying to this case of capital net gain the capital net loss doctrine of the *Elkins* case). The latter course would surely defeat the desirable and wise policy of allowing 15 per centum of the net taxable income to flow tax-free to charity in those years in which the taxpayer is most able to make charitable donations.

VI

CONCLUSION

It is respectfully submitted that the term "net income," as used in Section 23 (*n*) of the Revenue Act of 1928, means the total net income subject to tax, as computed before the deduction for charitable gifts, and includes a capital gain.

Furthermore, it is submitted that the inclusion of capital net gain in the "net income" upon which the charitable gifts deduction is computed, is in line with sound public policy and consistent with the purpose of the Revenue Act to foster the support of charity by the contributions of private individuals.

Respectfully submitted,

PHILLIPS KETCHUM,
Counsel for Robert Treat Paine, 2nd.
1 Federal Street,
Boston, Massachusetts.